



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF
CHIEF COUNSEL

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[REDACTED]

Reference: [REDACTED]

[REDACTED]

This letter is in response to your letter, dated June 27, 2002, on behalf of [REDACTED] seeking relief from an inadvertent S corporation status termination due to the issuance of stock to an ineligible shareholder.

Section 1361(a)(1) of the Internal Revenue Code defines a S corporation as a small business corporation for which an election under section 1362(a) is in effect. Section 1361(b)(1) defines "small business corporation" as a domestic corporation that is not an ineligible corporation and that does not (A) have more than 75 shareholders, (B) have as a shareholder a person (other than an estate, other than a trust described in section 1361(c)(2), and other than an organization described in (c)(6)) who is not an individual, (C) have a nonresident alien as a shareholder, and (D) have more than one class of stock.

Section 1362(f) of the Code provides that a corporation is treated as continuing to be a S corporation during the period specified by the Secretary if (1) an election under section 1362(a) by any corporation was terminated under paragraph (2) or (3) of section 1362(d), (2) the Secretary determines that the termination was inadvertent, (3) no later than a reasonable period of time after discovery of the terminating event, steps were taken so that the corporation is once more a small business corporation, and (4) the corporation, and each person who was a shareholder of the corporation at any time during the period specified pursuant to section 1362(f), agrees to make any adjustments (consistent with the treatment of the corporation as an S corporation) as may be required by the Secretary with respect to that period.

Section 1.1362-4(c) of the Income Tax Regulations clearly states that a corporation that believes that its S corporation status was inadvertently terminated must request a private letter ruling from the Internal Revenue Service granting relief from the

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inadvertent termination. The regulations require that all relevant facts pertaining to the event, including but not limited to, the facts described in paragraph (b) of this section, the date of the corporation's election under section 1362(a), a detailed explanation of the event causing termination, when and how the event was discovered, and the steps taken to return the corporation to small business status be presented by the taxpayer in the ruling request.

Additionally, sections 1.1362-4(d) and (e) of the regulations provide that the Commissioner may require any adjustments that are appropriate. As such, the regulations require that the corporation and all shareholders at any time during the period specified by the Commissioner must consent in writing to any adjustments the Commissioner deems appropriate. Each consent should be in the form of a statement agreeing to make the adjustments. The statement must be signed by the shareholder (in the case of a shareholder consent) or a person authorized to sign the return required by section 6037 (in the case of corporate consent). (Section 1.1362-6(b)92) provides information regarding persons required to sign consents.) The regulations also provide that the shareholder's consent statement should include the name, address, and taxpayer's identification numbers of the corporation and shareholder, and the dates on which the shareholder owned any stock. The corporate consent statement must include the name, address, and taxpayer identification numbers of the corporation and the shareholders.

Finally, the regulations specify that in the case of a transfer of stock to an ineligible shareholder that causes the inadvertent termination under section 1362(f) of the Code, the Commissioner may require the ineligible shareholder to be treated as a shareholder of an S corporation during the period the ineligible shareholder actually held the stock in the corporation. See section 1.1362-4(d) of the Income Tax Regulations.

As stated above, in order to receive a determination from the Commissioner that the termination of a corporation's S election was inadvertent under section 1362(f) of the Code, the taxpayer must submit a valid and complete request for private letter ruling. The procedure for submitting such a request is outlined in Revenue Procedure 2002-01. For your convenience, we have included a copy of the Revenue Procedure with this letter.

Please note that there is a filing fee required, if you decide to seek a private letter ruling (see Appendix A of Rev. Proc. 2002-01, which is tabbed for your convenience). Appendix B provides a sample letter ruling format which should be followed. It contains a complete ruling request with descriptions of what is required. Finally, Appendix C is a required checklist that should be filled out and submitted with your private letter ruling request to ensure its completeness.

We appreciate this opportunity to provide you with assistance. If you have further questions, please contact us at (202) 622-3050 (not a toll free number).

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Sincerely,

/s/ Dianna K. Miosi

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Enclosure (1)
Revenue Procedure 2002-01